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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 950

GRANVILLE C. MORTON,

Petitioner,

vs.

KATE THOMAS, AS COMMUNITY SURVIVOR OF THE ESTATE OF W. A. THOMAS, DECEASED, FORMER COLLECTOR OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

HOMER JACK FISHER,
LLOYD E. ELLIOTT,
Counsel for Petitioner.

O. D. BRUNSON,
Of Counsel.

INDEX

Subject Index

	Page
Petition for certiorari	1
Summary statement of case	1
Jurisdiction	3
Question presented	3
Reasons relied on for allowance of writ	3
Prayer	4
Brief in support of petition for certiorari	5
Opinion of the Court below	5
Jurisdiction	5
Statement of the case	6
Specification of error	6
Summary of argument	6
Argument	7
Conclusion	9

Cases Cited

Black v. *Commissioner*, 114 F. (2d) 355	4, 6, 7
Burnet v. *Leininger*, 285 U. S. 136	8

Statutes

Section 240(a), Judicial Code, as amended by the Act of February 13, 1925, 43 Stat. 938, Title 28 U. S. C. A., Sec. 347	3
Section 181, Internal Revenue Code, 26 U. S. C. A. 181	10

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To the Honorable Fred M. Vinson, Chief Justice of the United States, and Associate Justices of the Supreme Court of the United States:

The petition of Granville C. Morton, would respectfully show to this Honorable Court:

I

Summary Statement of the Case

This was a suit for refund of income taxes paid to the Collector of Internal Revenue at Dallas, Texas, for the years 1938 to 1941, inclusive, and alleged to be due petitioner because of the erroneous inclusion by the petitioner

in his returns for the years indicated, of income attributable to a 60% interest in a partnership known as Morton Potato Chip Company, one-half of which interest and the income therefrom belonged, by operation of law, to his daughter, Loumelia Jane Morton.

Prior to August 13, 1938, petitioner owned a 60% interest in the partnership known as Morton Potato Chip Company (R. 36). This interest was community property of petitioner and his wife. On August 13, 1938, the wife died intestate. No administration was had on her estate. Under the law of the State of Texas her community one-half of such partnership interest passed to and vested in the daughter of said marriage, Loumelia Jane Morton, then eleven years of age.

The interest of petitioner and his wife in the partnership at the time of the death of the wife was worth $25,000 (R. 34). Thereafter petitioner withdrew from the firm only such amount as was necessary for bare living expenses (R. 39), so that by accumulating the balance the Morton interest was worth $220,000 by the end of 1945.

Prior to the death of his wife, petitioner was accustomed to making joint returns for himself and his wife (R. 35). After her death he continued to return all the income attributable to the Morton 60% interest and to pay the tax due on the whole thereof until January, 1944, when he began making separate returns in which he reported one-half of the income as his daughter's. Also, at that time, he went back and filed returns for his daughter for the years 1938 to 1941, inclusive, and made claim for refund for the taxes paid by him upon the income properly taxable to his daughter upon that basis (R. 35, 37, 11, 16, 22 and 27).

Claim for refund being denied by the Commissioner on October 5, 1945 (R. 29), suit was in due time filed against the legal representative of the Collector of Internal Revenue in the United States District Court at Dallas, Texas.

Judgment for the defendant (R. 48) was affirmed by the Circuit Court of Appeals for the Fifth Circuit at New Orleans on the holding that under Section 181 of the Internal Revenue Code (26 U. S. C. A. 181) "the only persons taxable on income from a partnership are the partners," wherefore, since the daughter was not a partner, petitioner must pay the taxes on that portion of the income attributable to the interest the daughter inherited from her mother (R. 55).

II

Jurisdiction

The date of the judgment to be reviewed is December 6, 1946 (R. 56). A motion for rehearing in the Circuit Court of Appeals (R. 57-61) was overruled January 7, 1947. The jurisdiction of this Honorable Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925, 43 Stat. 938, Title 28 U. S. C. A., Sec. 347, and Supreme Court Rule 38, Sec. 5(b).

III

The Question Presented

The question here presented is whether Section 181 of the Internal Revenue Code (26 U. S. C. A., 181) (set out in full in the Appendix to the brief in support hereof), requires a partner to pay the tax attributable to the partnership interest standing in his name notwithstanding another has succeeded by operation of law to one-half of such interest.

IV

Reasons Relied on for Allowance of Writ

1. The decision of the Circuit Court of Appeals is in conflict with the decision of the Circuit Court of Appeals for

the Ninth Circuit in *Black* v. *Commissioner* (1940), 114 F. (2d) 355.

2. The Circuit Court of Appeals has decided an important question of Federal law which has not been, but should be, settled by this Honorable Court, in that there is now a conflict between the Circuit Courts of Appeals on the question involved, and the decision of the Circuit Court of Appeals in this case, in holding that ownership of income, resulting from inheritance of corpus and not from mere assignment, is not the test of taxability merely because such income is partnership income, will make for interminable confusion in the administration of the law.

WHEREFORE, petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the Circuit Court of Appeals for the Fifth Circuit at New Orleans, commanding that court to certify and send to this Court for its review and determination, on a date certain therein to be named, a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket as No. 11,779, Granville C. Morton, Petitioner, *vs.* Kate Thomas, as Community Survivor of the Estate of W. A. Thomas, Deceased, Former Collector of Internal Revenue, Respondent, that said judgment of said court may be reversed by this Honorable Court, and that petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just, and your petitioner will ever pray.

GRANVILLE C. MORTON,
By HOMER JACK FISHER,
LLOYD E. ELLIOTT,
Dallas, Texas.

O. D. BRUNDIDGE,
Of Counsel.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1946

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GRANVILLE C. MORTON,

vs. *Petitioner,*

KATE THOMAS, AS COMMUNITY SURVIVOR OF THE ESTATE OF W. A. THOMAS, DECEASED, FORMER COLLECTOR OF INTERNAL REVENUE *Respondent.*

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

I

The Opinion of the Court Below

The Opinion of the Trial Judge (R. 46-47) was delivered orally and has not been reported. The Opinion of the United States Circuit Court of Appeals (R. 53-56) has not been officially reported. It is reported in CCH 47-1 USTC, Paragraph 9101.

II

Jurisdiction

The basis upon which it is contended that this Court has jurisdiction to review the judgment is set forth under Paragraph 2 of the Petition to which reference is made.

III

Statement of the Case

The case has already been stated, pages 1 and 2, in the Petition, which is hereby adopted and made a part of this brief.

IV

Specification of Error

The Honorable Circuit Court of Appeals erred in holding that Section 181 of the Internal Revenue Code requires petitioner, as a member of the partnership of Morton Potato Chip Company, to return and pay a tax upon all of the income from the Morton interest in said partnership, notwithstanding his daughter had succeeded by operation of law to absolute ownership of the corpus of one-half of such partnership interest, and under the local law of Texas was the actual beneficial owner of one-half of such income.

V

Summary of the Argument

The holding of the Circuit Court of Appeals that petitioner, as a partner in the Morton Potato Chip Company, was required by force of Section 181 of the Internal Revenue Code to return all of the income attributable to the Morton interest in the partnership and pay the entire tax thereon, notwithstanding the daughter owned one-half of such interest, is in conflict with the holding of the Ninth Circuit Court of Appeals in the case of *Black* v. *Commissioner* (1940), 114 F. (2d) 355.

Argument

The Honorable Circuit Court of Appeals in this case states that: "The case is a very simple one, and we think it quite clear that the District Judge was right.

"Under the applicable provisions of the Internal Revenue Code [Sec. 181], the only persons taxable on income from a partnership are the partners. It is not claimed that Loumelia was a partner. On this record it could not be. In addition to the fact that she is a minor and can not make a binding agreement, there is not one syllable of testimony that she ever agreed, or that anybody agreed for her, to act as, or be, a partner. Morton and Mitchell are the only partners. They, and they alone, must return and pay the tax on income from the partnership."

The Ninth Circuit Court of Appeals in *Black* v. *Commissioner* (1940), 114 F. (2d) 355, construed Section 181 here involved as meaning no more than that income from a partnership was taxable to the partners in their individual capacity and not to the firm as an entity, and hence, as not requiring a partner to pay a tax upon income from the entire partnership interest standing in his name where such income was partly owned by another.

Pertinent language from the decision is found on page 359, as follows:

> "Here the partnership filed the usual information returns, but it paid, and was required to pay, no tax. Individuals carrying on business in partnership are liable for income taxes in their individual capacity only. Sec. 181, Revenue Act of 1934, c. 277, 48 Stat. 680, 730, 26 U. S. C. A. Int. Rev. Acts, p. 728. Each partner, in computing his net income, is required by Sec. 182, of the act, 26 U. S. C. A. Int. Rev. Acts, p. 728, to report his distributive share of the net income of the partnership, whether distributed to him or not.

"In view of the language of the statute, we are not disposed to interpret it as meaning that the entire amount of income distributable to a partner is taxable to him, even though half of it is owned by his wife. The better interpretation of the provisions referred to would seem to be that, in cases involving community income, the tax is imposed on the individual partner to the extent only of his ownership of the income. Compare Blair *v.* Commissioner, 300 U. S. 5, 12, 57 S. Ct. 330, 81 L. Ed. 465. This seems to be the Commissioner's construction, since Art. 181-1, Regulations 86, promulgated under the 1934 Act direct that 'if separate returns are made by the husband and wife domiciled in a community property state; and the husband only is a member of a partnership, that part of his distributive share of the partnership's net income which is community property should be reported by the husband and by the wife in equal proportions.' "

This decision of the Ninth Circuit involved an ownership by the wife of one-half of the partnership interest and its income, arising from the operation of community property laws. The ownership of the daughter in the instant case is no less, and its source is likewise the law of the domicile of the parties.

The Circuit Court of Appeals in the instant case, cites in support of its holding, that partnership income must be taxed to the partners, the decision of this Honorable Court in *Burnet* v. *Leininger,* 285 U. S. 136, whereas, the Circuit Court of Appeals in the *Black* case did not consider that *Burnet* v. *Leininger* required such holding because, said the court: "The view taken is not, we think, inconsistent with *Burnet* v. *Leininger,* 285 U. S. 136, 141, 53 S. Ct. 345, 76 L. Ed. 665. In that case there had been no transfer of the partnership assets but a mere assignment of part of the distributive share of the partner."

The Circuit Court of Appeals for the Ninth Circuit apparently took notice of the fact that this Honorable Court in *Burnet* v. *Leininger,* 285 U. S. 186, observed that

in the *Leininger* case "There was no transfer of the corpus of the partnership property to a new firm," and that, in the instant case, the "right of the wife was derived from the agreement with her husband and rested upon the distributive share which he had, and continued to have, as a member of the partnership." The Circuit Court of Appeals for the Fifth Circuit in the instant case, looking only to certain language contained in the opinion, construed the decision in the *Leininger* case as justifying the holding that Section 181 of the Internal Revenue Code requires that all of the income of a partnership must be taxed, at all events, to the partners without regard to actual ownership of such income.

There is, therefore, not only a conflict between the decisions of the Circuit Courts of Appeals as to the construction of Section 181 of the Internal Revenue Code, but likewise a conflict over the construction which this Honorable Court has placed upon such Statute.

For these reasons, and because of the confusion that would inevitably result from this improper application of the doctrine of *Burnet* v. *Leininger* to cases in which ownership of a portion of a partnership interest and its income actually lies in someone other than a partner and has been acquired by operation of law and not by assignment, and because of the confusion that would result from an attempt to apply to partnership income a rule different from that governing in the case of beneficial ownership of income generally, this Honorable Court should grant the writ of certiorari, and thereafter review and reverse the decision of the Honorable Circuit Court of Appeals.

Respectfully submitted,

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O. D. BRUNDIDGE,
Of Counsel.

APPENDIX

Sect. 181. Partnership not taxable

Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity. 53 Stat. 69.

Sect. 182. Tax of partners

In computing the net income of each partner, he shall include whether or not distribution is made to him—

(a) As part of his gains and losses from sales or exchanges of capital assets held for not more than 6 months, his distributive share of the gains and losses of the partnership from sales or exchanges of capital assets held for not more than 6 months.

(b) As part of his gains and losses from sales or exchanges of capital assets held for more than 6 months, his distributive share of the gains and losses of the partnership from sales or exchanges of capital assets held for more than 6 months.

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183(b). 53 Stat. 69, as amended Oct. 21, 1942, 4:30 p. m., E.W.T., c. 619, title 1 Sec. 150(g) (1), 56 Stat. 845.

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statutes involved	2
Statement	3
Argument	4
Conclusion	9

CITATIONS

Cases:	
Black v. *Commissioner*, 114 F. 2d 355	7, 8
Burnet v. *Leininger*, 285 U. S. 136	5, 6
Commissioner v. *Tower*, 327 U. S. 280	7
Larsen v. *Burnet*, 50 F. 2d 308	5
Lusthaus v. *Commissioner*, 327 U. S. 293	7
Statutes:	
Internal Revenue Code:	
Sec. 181 (26 U. S. C. 1940 ed., Sec. 181)	2, 4
Sec. 182 (26 U. S. C. 1940 ed., Sec. 182)	2, 5
Revenue Act of 1938, c. 289, 52 Stat. 447:	
Sec. 181	2
Sec. 182	2

In the Supreme Court of the United States

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 46–47) is not reported. The opinion of the Circuit Court of Appeals (R. 53–56) has not yet been reported.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on December 6, 1946. (R. 56.) A petition for rehearing (R. 57–61) filed on December 21, 1946 (R. 57), was denied on January 7, 1947 (R. 62). The petition for a writ of certiorari was filed on January 24, 1947. The juris-

diction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the court below correctly held that the taxpayer's distributive share of partnership earnings was taxable to him and that his daughter was not shown to have such an interest therein that any portion of that income could be attributable to her for tax purposes.

STATUTES INVOLVED

Internal Revenue Code:

> SEC. 181. PARTNERSHIP NOT TAXABLE.
>
> Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.
>
> (26 U. S. C. 1940 ed., Sec. 181.)
>
> SEC. 182. TAX OF PARTNERS.
>
> In computing the net income of each partner, he shall include, whether or not distribution is made to him—
>
> * * * * *
>
> (c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183 (b).
>
> (26 U. S. C. 1940 ed., Sec. 182.)

The provisions of Sections 181 and 182 (c) of the Revenue Act of 1938, c. 289, 52 Stat. 447, are identical with the corresponding provisions of the Internal Revenue Code quoted above.

STATEMENT

This suit was brought for the refund of a portion of income taxes paid for the years 1938 through 1941, the taxpayer claiming that one-half of the income he had reported as derived from a partnership was not taxable to him but should have been taxed to his daughter. (R. 2, 5–6.) The taxpayer resides and has his place of business in Dallas, Texas. (R. 1–2, 30.)

The taxpayer was the only witness and his testimony was to the following effect (R. 32–42): In 1932 he established a business known as the Morton Potato Chip Company. This was done with community property and community efforts. In 1937 L. M. Mitchell was admitted into the business, he and the taxpayer being associated as partners, and the profits being shared on the basis of 40 percent to Mitchell and 60 percent to the taxpayer. (R. 54.)

In 1938 the taxpayer's wife died. At that time their share of the partnership assets was worth approximately $27,000; at the time of the trial of this case the assets of the business were greatly enhanced in value. Prior to the time that his wife died, the taxpayer's share of the earnings from the business was considered as community property and he and his wife paid their federal income taxes on that basis. (R. 54.)

After the death of his wife and until 1944, the partnership continued without change and the

taxpayer, both on the partnership books and in his income tax returns, treated 60 percent of the income from the partnership as his own. In 1944, after having been advised by a tax expert, the taxpayer started making tax returns on the basis that only 30 percent of the partnership income was taxable to him and that 30 percent was taxable to his daughter. He also filed, on January 19, 1944, claims for refund of part of the taxes paid for the period 1938 through 1941 on the ground that a one-half interest in the partnership assets and profits devolved upon his daughter at the death of his wife. (R. 7–28, 54.) These claims were rejected on October 5, 1945 (R. 29), and the taxpayer then filed this suit to recover the amounts allegedly overpaid. The District Court entered judgment against the taxpayer (R. 48–49) and, on appeal, the judgment was affirmed by the Circuit Court of Appeals (R. 56). Because it decided that the taxpayer had not made any overpayment, the court below did not pass on the holding of the District Court (R. 46) that the claims for refund for 1938 and 1939 were in any event barred by Section 322 of the Internal Revenue Code.

ARGUMENT

1. The decision of the Circuit Court of Appeals is correct.

Under Section 181 of the Internal Revenue Code, *supra*, individuals carrying on business in

partnerships are made liable for income tax in their individual capacity, and under Section 182 (c), *supra*, each partner is required to include in the computation of his net income his distributive share of the ordinary net income of the partnership whether or not distribution is made to him.

The court below has properly observed (R. 55) that no valid contention has been or could be made that the taxpayer's daughter was a partner in the partnership business carried on by the taxpayer and Mitchell, for there is no testimony whatsoever that she ever agreed, or that anybody agreed for her, to act as, or be, a partner. The determination of the District Court (R. 47) that the only partners were the taxpayer and Mitchell was therefore correctly affirmed by the court below. Under the plain language of the statute the entire income of the partnership is taxable to these two partners, and the taxpayer accordingly correctly returned his 60 percent distributive share as his income in the taxable years here involved. *Burnet* v. *Leininger*, 285 U. S. 136; *Larsen* v. *Burnet*, 50 F. 2d 308 (App. D. C.).

The taxpayer contends, however (Br. 6), that his daughter had, upon the death of her mother in 1938, succeeded by operation of law to absolute ownership of the corpus of one-half of his partnership interest and under the local law of Texas was the actual beneficial owner of one-half of the taxpayer's distributive share of the partnership's

income and hence that the taxpayer was not taxable on this portion of the income. A similar contention was rejected by this Court in *Burnet* v. *Leininger, supra,* where this Court said (p. 141):

> The respondent urges that the assignment to his wife was of one-half of the *"corpus"* of his interest and that this *"corpus"* produced the income in question. The characterization does not aid the contention. That which produced the income was not Mr. Leininger's individual interest in the firm, but the firm enterprise itself, that is, the capital of the firm and the labor and skill of its members employed in combination through the partnership relation in the conduct of the partnership business. There was no transfer of the *corpus* of the partnership property to a new firm with a consequent readjustment of rights in that property and management. If it be assumed that Mrs. Leininger became the beneficial owner of one-half of the income which her husband received from the firm enterprise, it is still true that he, and not she, was the member of the firm and that she had only a derivative interest.
>
> The statute dealt explicitly with the liability of partners as such. [Referring to Section 218 (a) of the Revenue Acts of 1918, c. 18, 40 Stat. 1057, and 1921, c. 136, 42 Stat. 227, now Section 181 of the Internal Revenue Code.] Applying to this case, the statute provided that there should be included in computing the net income of

> Leininger his distributive share of the net income of the partnership. That distributive share, as he himself stated in his return on behalf of the partnership, was one-half. In view of the clear provision of the statute, it cannot be said that Leininger was required to pay tax upon only a part of this distributive share because of the assignment to his wife. * * *

See also *Commissioner* v. *Tower,* 327 U. S. 280; *Lusthaus* v. *Commissioner,* 327 U. S. 293.

Under the record in the present case, as made, no question is presented with respect to the right of the taxpayer to an offsetting deduction because of any liability of either himself or of the partnership to the taxpayer's daughter because of the use in the partnership business of any property of hers, nor is the amount of any such supposed liability shown by the record. The court below accordingly properly held (R. 54–55) that these questions are without bearing on the determination of the question involved.

2. *Black* v. *Commissioner,* 114 F. 2d 355 (C. C. A. 9th), which the taxpayer relies on (Br. 7–9) is not in conflict with the decision below. The income there in question was derived from certain farm land in the State of Washington which the taxpayer and his brother had acquired from their parents. The taxpayer's share of such land was held by the court (p. 357) to be the community property of the taxpayer and his wife. The tax-

payer and his brother entered into a partnership to *operate* the land, the court pointing out (p. 358) that the partnership did not own the land. The court held (p. 359) that the portion of the income attributable to the community land itself to which the taxpayer's wife was entitled, was not taxable to her husband but that the portion of the partnership income attributable to the personal services of the taxpayer was taxable to him alone. In the present case, the taxpayer's daughter had no interest similar or analogous to the interest of the taxpayer's wife in the *Black* case. The partnership business involved here was completely different from a partnership to operate land, title and ownership of which was not in the partnership. Here the partnership owned the assets employed in the partnership business with, at most, a right on the part of the taxpayer's daughter to an accounting. For all that the record in the present case shows, the income of the partnership here involved may have been attributable primarily to the personal efforts and skill of the two partners, rather than to the capital employed in the partnership. There has been no effort on the part of the present taxpayer to establish what portion of the partnership's income was attributable to the capital employed by the partnership. Clearly the taxpayer's daughter was not entitled to a distributive share of the partnership's income as such, and accordingly there is no basis for a

contention that the taxpayer's distributive share should not be included in the computation of his net income as provided by the statute.

CONCLUSION

The decision below is correct. No conflict in decisions is presented. Accordingly, further review of the case would not be warranted, and the petition for a writ of certiorari should be denied.

Respectfully submitted.

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FEBRUARY, 1947.

U. S. GOVERNMENT PRINTING OFFICE: 1947